No. 12846

United States Circuit Court of Appeals

For the Ninth Circuit

CHARLES D. BRONSON, JR.,

Appellant,

vs.

HUGH EARLE, Collector of Internal Revenue for the District of Oregon and United States of America,

Appellees.

Appeal from the United States District Court for the District of Oregon

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BRIEF OF APPELLANT

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BRIEF OF APPELLANT

STATEMENT OF PLEADING AND FACTS UPON WHICH JURISDICTION IS BASED

Plaintiff commenced this action in the United States District Court for the District of Oregon against Hugh Earle, Collector of Internal Revenue for the District of Oregon, and The United States

of America for the recovery of Federal Income taxes alleged to have been erroneously and illegally assessed against and collected from plaintiff.

The Collector of Internal Revenue to whom $19,415.25 of said taxes was paid was not in office at the commencement of the action (Tr. p. 4).

The Collector of Internal Revenue to whom $6,281.89 of said taxes was paid was the duly acting, constituted and appointed Collector at the time this said action was commenced.

Jurisdiction of the United States District Court for the District of Oregon is grounded on congressional acts of June 25, 1948, Ch. 646 §1, 62 Stat. 933; April 25, 1949, Ch. 92 §2 (a), 63 Stat. 62; and May 24, 1949, Ch. 139 §80 (a), (b), 63 Stat. 101, Federal Code Title 28 Sections 1340 and 1346.

Jurisdiction of this court is grounded on Congressional Act of June 25, 1948, Ch. 646 §1, 62 Stat. 929, Federal Code Title 28, Section 1291 and Congressional Act of June 25, 1948, Ch. 646 §1, 62 Stat. 930, Federal Code Title 28, Section 1294.

Jurisdiction is stated in paragraph I of plaintiff's complaint (p. 1—Cert. Trans. of record), and

in paragraph I of defendants' answer, jurisdiction is admitted.

STATEMENT OF CASE

There are only two fundamental questions involved in this litigation:

1. Did the Commissioner of Internal Revenue err in determining that one-half of the income from a partnership known as Parkdale Lumber Company, Oreg. Ltd. should be taxed to plaintiff rather than one-fourth of said income, and

2. Did the Commissioner of Internal Revenue err in determining that all of the income from a co-partnership known as Ashbaugh Shingles and Shakes should be taxed to plaintiff rather than to plaintiff's wife (Tr. p. 6).

The disputed questions involve interpretation of the law relative to so-called family partnerships as applied to the peculiar facts of this case, and interpretation of the law relative to taxability of income as an assignment from an entity in which taxpayer did not own nor control any interest.

There are two separate and distinct partnerships in question.

PARKDALE LUMBER COMPANY was formed in 1944 as a limited partnership in which plaintiff and Janet Roles were limited partners and plaintiff's wife, Mildred P. Bronson, and R. C. Roles were the general partners, with the place of business at Parkdale, Oregon, to engage in the manufacture of lumber.

ASHBAUGH WOOD SHINGLES & SHAKES was formed in 1945 as a partnership with Morgan Stark, Lavinia Stark, B. C. Roos, Frank Belcher, Janet Roles and Mildred Bronson, as partners, with the principal place of business at Los Angeles, California, to engage in the sale of wood shingles and shakes.

Mr. and Mrs. Roles resided near Toledo, Oregon, Mr. and Mrs. Bronson, at Parkdale, Oregon, and Mr. and Mrs. Stark, Mr. Roos and Mr. Belcher resided at Los Angeles, California.

As to the certain income from Parkdale Lumber Company Oreg. Ltd. the commissioner allocated an additional one-fourth of the income from Parkdale Lumber Company to plaintiff and assessed and collected an additional tax based thereon and credited plaintiff with an offset to the extent of the

tax previously paid by plaintiff's wife on such income (the total income allocated to plaintiff after said addition being one-half of the total income of Parkdale Lumber Company). (Pretrial Order, Par. IX—Tr. p. 6.)

As to the certain income from Ashbaugh Wood Shingles and Shakes, the Commissioner assessed and collected from plaintiff a tax based on the assessment to him of the full amount of the income of that partnership on which Mildred P. Bronson had previously paid the tax and credited plaintiff with an offset to the extent of the taxes previously paid on this income by Mildred P. Bronson. (Pretrial Order, Par. IX—Tr. p. 6.)

The amounts involved are not in dispute and are admitted in the pretrial order (Tr. p. 3-6) wherein it is stipulated that on the trial of the case in the event of a judgment for plaintiff, the amounts will be fixed by agreement or by subsequent order of the court. (Pretrial Order, Par. XI—Tr. p. 6.)

CONTENTION OF APPELLANT

1. Plaintiff contends that the Commissioner erred in the determination relative to the alloca-

tion of the income previously reported by plaintiff's wife, and that plaintiff is entitled to a refund of the taxes paid as a result of said allocation to him, and that the court erred in entering findings of fact and conclusions of law to the contrary and in entering judgment thereon.

2. That there can be no arbitrary allocation of income between partners (two of whom were unrelated to the remaining two) in a new and untried business venture under the facts of this case.

3. That the income from a business in which plaintiff had no financial investment, nor right of control or management or no interest either in the investment or income can not be taxed to him for income tax purposes, but must be taxed according to the agreement of the partners, and that the court erred in entering findings of fact and conclusions of law in the contrary and in entering judgment thereon.

4. That there was insufficient evidence to support the findings of fact entered by the court and each of them.

5. That the conclusions of law are not in accordance with law and are against the weight of

authority and the evidence.

6. That there can be no reapportionment of income within the family group where there was no income to apportion when the partnership was formed.

7. That said partnership could not have been formed for tax purposes solely when there was no income to be taxed.

8. That where a new business venture is formed, the judgment of the parties is conclusive as to the value of services to be rendered by the partners.

9. That if a partnership is valid for any purpose, it is valid for tax purposes save and except where its sole purpose is the avoidance of taxation.

10. That a corporation can not be a lawful partner.

11. That a person can not assign something which he never had the right to control.

These questions are raised by the pretrial order "contentions of plaintiff" (Tr. p. 7) and objections to finding of fact and conclusions of law (Tr. p. 15-17) and by plaintiff's designation of points on file herein.

SPECIFICATIONS OF ERROR RELIED UPON

Appellant contends that the court erred:

I. In entering the conclusions of law as follows, over plaintiff's objections thereto and in entering judgment thereon as being contrary to law and to the evidence as applied thereto (Tr. pages 14 and 15).

a. Plaintiff has failed to sustain the burden of proof on the issue that he and his wife, Mildred P. Bronson, were bona fide partners in the Parkdale Lumber Company.

b. The Commissioner of Internal Revenue properly taxed to the plaintiff one-half of the income from Parkdale Lumber Company for the taxable years herein involved.

c. The amounts of money paid to Mildred P. Bronson during the taxable years herein involved by Ashbaugh Wood Shingles and Shakes represented income of the plaintiff assigned by plaintiff to his wife, Mildred P. Bronson. Such amounts were property taxed to plaintiff.

II. In entering findings of fact over plaintiff's objections thereto and in basing conclusions of law and judgment thereon as follows:

a. Appellant contends that findings of fact number 2 (Tr. p. 10) is erroneous in that the evidence discloses that a contribution to the capital of the Parkdale Lumber Company partnership was made by each of the partners thereto.

b. Appellant contends that the finding of fact numbered 3 (Tr. p. 10) is erroneous in that the evidence discloses that Mildred P. Bronson did contribute services to the partnership.

c. Appellant contends that the finding of fact numbered 4 (Tr. p. 10) is erroneous in that the same states a conclusion and is not factual upon which an objection could be predicated and is not supported by the evidence in that investment and management was not vested solely in plaintiff.

d. Appellant contends that the findings of fact numbered 5 (Tr. p. 11) is erroneous in that the evidence discloses that defendant did not receive or actually control and treat as his own all of the Parkdale income taxed to him, but on the contrary treated no more than one-half of said income as his own, and that the control of said money was divided between appellant and his wife, and further appellant received only one-fourth of the income from this source.

e. Appellant contends that findings of fact number 6 (Tr. p. 11) is erroneous in that the evidence discloses that there was in fact at the formation of Parkdale Lumber Co. partnership no family economic relationship as to income which would be the subject of change, and that appellant at the formation of the contract had not produced nor earned any income from the partnership business, and further that appellant had no right to control the use and disposition of any of the partnership earnings, except his own one-fourth interest.

f. Appellant contends that findings of facts numbered 7 (Tr. p. 1) is erroneous in that the finding that Mildred Bronson did not in any substantial manner influence the conduct of the business of Parkdale Lumber Company is without support in the evidence, and further contends that the finding that Mildred P. Bronson did not exercise any voice or control of the distribution of income from the business is erroneous in that there is no evidence to support said finding.

g. Appellant contends that finding of fact number 8 (Tr. p. 11) is so broad as to be a conclusion and not sufficient or definite to be subject to an objection on factual grounds disclosed by the evi-

dence, and is contrary to any evidence in that the control of the partnership was always vested in a majority thereof, and that the legal right to control of the business was vested in Mildred P. Bronson and R. C. Roles.

h. Appellant contends that the finding of fact numbered 9 (Tr. p. 11) is erroneous in that the same contains a series of facts and appears to be a conclusion based on said facts and is therefore not subject to an objection on factual grounds, but that the evidence does not disclose facts from which such a conclusion should be reached, and that the evidence discloses that the parties did intend to and did join together in the conduct of the partnership business.

i. Appellant contends that the finding of fact numbered 10 (Tr. p. 11) is erroneous in that the same is unsupported in the evidence in that no partner in the business was brought into the partnership, but rather the partnership was organized prior to the commencement of its operation and further that no partner could be brought into the business for the purpose of minimizing taxes based on income at the inception of said business, when

at such time there was no income to tax either to appellant or any other partner.

j. Appellant contends that finding of fact 12 (Tr. p. 13 and 14) is erroneous in that there is no evidence to support the various factual elements contained therein and that if the income was taxable to plaintiff and assigned to his wife, his wife would have been equally taxable if assigned for value, on said income; however, her taxes based on this income were refunded to her and the question of assignment is thereby waived; and further that since appellant had no right to control the partnership income and had no interest therein that he had nothing to assign, nor could appellant have been taxed on the basis of right of management of the business or its policy nor on invested capital; since he contributed no capital, control, interest nor management.

SUMMARY OF ARGUMENT

Plaintiff summarizes his argument as follows:

Re: Parkdale Lumber Company

1. This partnership was originated and composed of four members, two members of two families, to engage in a new and untried business ven-

ture. It was therefore not formed for the sole purpose of avoiding income taxes since there was no income to avoid at its formation, and is therefore a valid partnership for Federal Income Tax purposes, and the allocation of a one-fourth share of the income from this source was arbitrary and capricious and without foundation in fact.

2. The facts as supported by the evidence disclose a contribution of capital, services and stability by the wife of plaintiff to the partnership and the parties intended in good faith to enter into a partnership for a business purpose.

Re: Ashbaugh Wood Shingles & Shakes

1. Income from a partnership venture in which plaintiff had no right of control or management, no capital investment, and no actual interest as a member thereof can not be taxed to plaintiff as a beneficiary.

ARGUMENT

THE SPECIFICATIONS ARE CONSIDERED SEPARATELY AS FOLLOWS:

I

That the conclusions of law are erroneous as follows:

A. PLAINTIFF HAS SUSTAINED THE BURDEN OF PROOF ON THE ISSUE THAT HE AND HIS WIFE, MILDRED P. BRONSON WERE BONA FIDE PARTNERS IN THE PARKDALE LUMBER COMPANY.

It was said by our Supreme Court (Frankfurter specially concurring) in the leading case of Culbertson vs. Commission, 69 S. Ct. 1210, 337 U. S. 733:

> "We should leave no doubt in the mind of the Tax Court, of Courts of Appeals, of the Treasury and of the bar that the essential holding of the Tower case is that there is 'no reason' why the 'general rule' by which the existence of a partnership is determined 'should not apply in tax cases where the Government challenges the existence of a partnership for tax purposes'."
>
> Culbertson vs. Commission 69 S. Ct. 1210, 337 U. S. 733, at page 1220.

It would appear therefore that if the facts of the present case indicate the existence of a partnership under the general rules, that is sufficient to sustain any burden of proof cast on plaintiff.

In discussing this question, it must be noted that this was not a case of "bringing in" to an existing business a family member for the purpose of diluting or reducing the income to a single family member without changing the economic status of the

family group, but rather the parties to the partnership of Parkdale Lumber Company, Oreg. Ltd. entered into the partnership arrangement prior to the conduct of any business. There is no evidence to the contrary. The certified copies of the articles are on file (Exhibits No. 25 and 26 and 23. This is the uncontradicted testimony of the parties (Tr. Plaintiff Tr. p. 46-77).

The facts of this case are likewise distinguishable from the usual situation in that in this case the partners were not all members of the same family or family group.

It must therefore be assumed that if there is no evidence to the contrary, that the plaintiff has carried any burden of proof required to establish the existence of a bona fide partnership.

It should also be pointed out that once plaintiff has proved such an ordinarily valid partnership arrangement, he has sustained his burden and the burden of proving to the contrary or of going forward should rest with the Commissioner.

The definition of a partnership is set forth in Section 79-201, Oregon Compiled Laws Annotated as follows:

> "A partnership is defined as an association of two or more persons to carry on as co-owners a business for profit."

And this is a generally accepted definition.

Section 79-705, Oregon Compiled Laws Annotated states:

> "Either a husband or wife may become and be either a general or limited partner with his or her spouse and other members either as general or limited partners. A limited partnership may carry on any business not prohibited by the laws of the State of Oregon."

It must therefore be assumed that Parkdale Lumber Company was a valid limited Oregon Limited partnership, there being no evidence to the contrary and if there is no special concept of a partnership for tax purposes, then this partnership was valid for tax purposes as well as other purposes.

If the parties intended to join together for the carrying on of a common enterprise and sharing in the profits and losses, then this partnership is valid for all purposes.

The fact that they did so intend is found in the evidence by the testimony of the parties and by the documentary evidence.

Documentary evidence:

Articles of Limited Partnership (Exh. No. 25 and 26).
State Report—Unemployment Compensation (Exh. No. 27).
Copy of Social Security Tax Return (Exh. No. 28).
Copy of Insurance Policy and Endorsement (Exh. No. 23 and 24).
Original Timber Sale Agreements with U. S. Forest Service and bond (Exh. No. 41 and 42).
Company Books (Exh. No. 43).
Partnership Income Tax returns (Exh. No. 104 and 107).

The testimony of the parties:

Charles D. Bronson, Tr. p. 45 and 46.

A. "There was just the four of us in the whole thing."

Q. "Can you state whether or not there were any discussions as to your conversations with Mr. Martin, between the other partners?"

A. "Oh, yes. There were discussions as to whether we could form this limited partnership or a corporation, just how to start."

Carey Martin Tr. p. 71.

A. ". . . It wasn't even discussed; but they had

the corporation which had two activities, of which Mr. and Mrs. Roles had been active in one of them and managed it and been there, and Mr. and Mrs. Bronson on the other. Now they had both contracted to buy another different operation (Parkdale Lumber Co.) . . ."

Richard Roles Tr. p. 123.

A. "The agreement was that we would all go in as partners and divide this Parkdale up equally between all."

There is no direct evidence to the contrary.

Therefore to hold to the contrary would be to substitute the judgment of the Commissioner for that of the parties.

This means that the Commissioner must have determined that Mr. and Mrs. Roles and Mr. Bronson did not intend to have Mrs. Bronson as a partner.

In other words, the Commissioner's judgment is being substituted for that of the people outside of the Bronson family.

It is sufficient for tax and other purposes if the judgment of the parties is that a partner add to the partnership in any manner whatsoever.

This reasoning was supported by one court in the following language.

"We can not subscribe to a doctrine which would say a person is not needed in a partnership. The people in the partnership may be the sole judge of what they need and outsiders may not say what is needed . . .

"We all know there are such partners as must be respected as silent partners not known to anybody. There are limited partners.

"Persons in partnership have a right to choose their business associates and if such person so chosen contributes to that partnership either in stability, money, capital, services, advice or what not, so that it is a real and actual benefit or contribution, then it comes within the dominatiing dimension of the Internal Revenue Act which relates to this matter as Congress intended that it should." J. L. Hair et ux. v. Arnold; C. B. Christie et ux. v. Arnold; Grover Ballington et ux v. Arnold, 501 U.S.T.C. Par. 9255.

"If upon a consideration of all the facts, it is found that the *partners* joined together in good faith to conduct a business, (the partners) *having agreed that the* services or capital to be contributed presently by each is of such value to the partnership that the contributor should participate in the distribution of profits, that is sufficient. The Tower case DID NOT PURPORT TO SUBSTITUTE ITS JUDGMENT FOR THAT OF THE PARTIES, it simply furnished some guides to the determination of their true intent." Culbertson vs. Commissioner (Supra, on page 1215) (Parenthesis and italics ours).

The partners of Parkdale Lumber Company, Oreg. Ltd. became acquainted in 1935 when they organized Warrenton Shingle Company, a corporation. All parties lived near the site of that company's mill and "lived with" its operation. The two families later separated to operate another shingle mill.

The original mill was destroyed by fire and the parties then discussed the purchase of another shingle mill or other investment and after considerable time and discussion, they then decided to purchase a lumber mill at Parkdale, Oregon.

The original payment came from individual funds of the parties and the agreement was signed in the name of the corporation until such time as the formal organization of the Parkdale Lumber Co., partnership was completed. All opening entries were made in the name of the partnership before operation was commenced. The original down payment was $10,000.00 and the partnership articles disclose capital contributions of $2,500.00 (one fourth of the original contribution which was to be equal).

The Court said in:

Lawton et al vs. Commission: 164 F. 2d 380, 385 quoted in Cooke vs. Glen (78 F. Supp.

519 (a), 528 Affirmed. Glen vs. Cooke (177 F. 2d 201).

"It would be strange also if in such a coordinated family activity, policies involving management sales and expansion were not discussed and decisions made at the family fireside."

B. THE COMMISSIONER OF INTERNAL REVENUE ERRED IN TAXING TO PLAINTIFF ONE-HALF OF THE INCOME FROM THE PARKDALE LUMBER COMPANY FOR THE TAXABLE YEARS HEREIN INVOLVED.

Since the partners of Parkdale Lumber Company intended to become partners in Parkdale Lumber Company, Oreg. Ltd. and did enter into an agreement therefor, the taxation of more than one-fourth of the Parkdale income to plaintiff was erroneous.

In the Culbertson case (Frankfurter specially concurring) (Supra), at page 1220, it was said:

"In plain English if an arrangement among men is not an arrangement which puts them in the same business boat, then they can not get into the same boat merely to seek the benefits of Section 181 and 182. But if they are in the same business boat, although they may have varying rewards and varied respective

responsibilities, they do not cease to be in it when the tax collector appears."

C. THE COMMISSIONER ERRED IN TAXING TO PLAINTIFF THE AMOUNTS OF MONEY PAID TO MILDRED P. BRONSON DURING THE TAXABLE YEARS HERE INVOLVED (1945 and 1946 only) BY THE ASHBAUGH WOOD SHINGLES AND SHAKES BECAUSE IT DID NOT REPRESENT INCOME OF PLAINTIFF ASSIGNED BY HIM TO HIS WIFE.

Plaintiff contends that the court's conclusion is clearly erroneous and contrary to the evidence and the law, as plaintiff did not at any time have any interest in or control over the management or income from the venture known as Ashbaugh Wood Shingles and Shakes.

The Commissioner contends, and the Court finds that this income is the income of the plaintiff.

Yet the plaintiff had never at any time had any interest financially in this partnership. It was created as the idea of one Morgan Stark and his attorney, Mr. Frank Belcher, an attorney of Los Angeles, California; it was an agreement between these parties in California and the wife of plaintiff and the wife of his business associate, Mr. Roles.

This was also an entirely new business venture, without knowledge of the future profits, if any, it would produce, and without management or right of management by plaintiff.

The profits which were distributed were profits from the sale of shingles in the Los Angeles area and these profits were not due in any respect to the efforts of Mr. Bronson. There is no evidence to the contrary.

Warrenton Shingle Company had been selling shingles to Ashbaugh Wood Shingles and Shakes while owned by Mr. Ashbaugh. When Mr. Ashbaugh sold his business to Beverly Roofing Company who assumed the same name, "Ashbaugh Wood Shingles and Shakes," the Warrenton Shingle Company continued to sell shingles to that company as before until it failed to pay for a shipment of shingles; therefor it refused to ship more until payment had been made.

It has been repeatedly held that where a business is entirely separate and distinct from a controlled corporation, the income of a partnership (family) is not taxable to the corporation, and in fact, in the case of John L. Denning & Co. Inc. vs. Commissioner 180 F. 2d 288) the husband was the

controlling stockholder of a corporation, but was not a member of a family partnership composed of wife, daughter and son who purchased broom corn and supplies from the same sources as the corporation and sold to the same customers. The wife and son contributed their own capital and the husband and wife loaned money to the daughter to invest in the business.

The Court of Appeals for the 10th Circuit held the corporation was not taxable on the income of the family partnership.

To the same effect, see Twin Oaks Co. vs. Commissioner (183 F. 2d 385, Ninth Circuit) where this court held that the Tax Court was in error in holding that the partial dissolution of a corporation with transfer of its assets to a family partnership was a sham to reallocate income (equivalent to assignment) and was therefore taxable on the partnership income.

Even if the capital of the Ashbaugh partnership had been contributed by plaintiff and he had relinquished control of his capital and income, the income could not be taxed to him. Bein 14 TC 1144, Vance 14 TC 1168.

To so hold would be to hold that a husband may be taxed on the income from a partnership in which his wife is a member merely by virtue of the family relationship.

The husband here had no right to control, made no investment, no contributions of services, was never a formal member, never intended to be a member formally or otherwise, shared none of the partnership income, nor any of its liability.

The plaintiff having nothing of value to assign, he can not be taxed as an assignor of income which may or may not be produced from a partnership of which he was not a member.

There is no basis in law or fact for the conclusion reached by the Trial Court or by the Commissioner.

If a partnership is recognized as valid, then the Commissioner has no authority to reallocate the income other than as agreed by the parties. Sol M. Fleck, 8 TC 945.

The validity of the Ashbaugh Wood Shingles and Shakes partnership is conceded by the Government in the deposition of Morgan Stark (Ex. No. 129, p. 36) when Mr. Winter states:

"We are not questioning the legality of your arrangements with the wives of Mr. Roles and Mr. Bronson. You have a perfect right to enter into an agreement with them."

II.

The findings of fact, and any conclusions or judgments based thereon are erroneous in that:

A. PLAINTIFF'S WIFE, MILDRED P. BRONSON, CONTRIBUTED CAPITAL DIRECTLY TO THE PARKDALE LUMBER COMPANY, (Finding No. 2, Tr. p. 10).

The evidence discloses that a contribution of capital to the Parkdale Lumber Company partnership was made by each of the partners thereto contrary to the finding.

The uncontradicted evidence discloses that Parkdale Lumber Company was purchased by the payment to the sellers of $10,000.00 as earnest money.

This money was paid by the check of Warrenton Shingle Company (whose stockholders were plaintiff and R. C. Roles) from funds of that company on hand at the time its original mill was completely destroyed by fire and in whose operation the stockholders and their wives had taken a very

active part. The certificate of limited partnership recites that the two limited partners, Mrs. Roles and plaintiff, had contributed $2,500.00 each.

Since we know that Mrs. Roles was not a stockholder in Warrenton Shingle Company and had no legal right to any part of the fund used for the down payment, it must appear that a gift of this capital was made to Mrs. Roles by Warrenton Shingle Company, and likewise, since the testimony disclosed that contributions were to be equal (Charles D. Bronson, Tr. p. 78), Mrs. Bronson's came from the same source.

Thus the original capital, while coming nominally from the Warrenton corporation, was $10,000.00 divided four ways or $2,500.00 by each partner.

The balance of the purchase price was paid from the profits of the business except for an additional $10,000.00 paid from the account of Mr. Bronson and Mr. Roles. These funds were treated as a loan.

> "Court: Did the Parkdale Lumber Company ever pay back in money to the Warrenton Shingle Company?
>
> "A. Yes, the Parkdale Lumber Company paid it back once, but we got a little on the bad

side at Parkdale and then took it back again." (Tr. p. 111).

The case of Apt vs. Birmingham, 89 Fed. Sup. 361, contains an excellent summary of the various holdings concerning "gift capital."

It has been repeatedly held that the amount contributed as capital, and income therefrom, may be considered the property of the donee for tax as well as general purposes.

Culbertson vs. Commissioner 69 S. Ct. 1270, 337 U. S. 733.
Apt vs. Birmingham 89 F. Sup. 361.
Kent vs. Commissioner 170 Fed. 131.
Huff vs. Glen 85 F. Sup. 386.
Graber vs. Commissioner 171 F. 2nd 32.
Willard vs. U. S. 89 F. Sup. 972.

In Apt vs. Birmingham, quoting Richardson vs. Smith, 102 F. 2d 697, 125 ALR 774, it was said:

> "The donor's mere belief, however well founded, that donee will permit him to control the subject matter of the gift and his purpose to do so are not sufficient in themselves to render the gift invalid or sham."

In the present case the capital investment made was not under control of the donor but under the control of the remaining three partners and in addition was subject to the rights of creditors as to Mrs. Bronson's share along with any other capital

contributions from loans or otherwise since she was a general partner in the business.

That there was a gift intended is further shown by the letters from Mr. Martin referring to gifts. (Tr. p. 55 and 56.)

The Supreme Court held in the case of Culbertson vs. Commissioner, supra, page 1216, "that facts may indicate on the contrary that the amount contributed and the income therefrom should be considered the property of the donee for tax as well as general law purposes."

In Cooke vs. Glen (78 F. Sup. 519, 530) it was said, "Although the capital contribution of Elva Cooke to Broadway Chevrolet originated with her husband V. V. Cooke, the amount borrowed was contributed to a *new venture* in the same proportion as V. V. Cooke, Almond Cooke and Jenny Cooke, the other partners, and in that proportion Elva Cooke is liable for Federal Income Taxes attributable to her one-fourth interest. (Emphasis ours.)

B. PLAINTIFF'S WIFE MADE A CONTRIBUTION OF SERVICES TO PARKDALE LUMBER COMPANY:

The evidence discloses that Mildred P. Bronson

did contribute services to the Parkdale Lumber Company, Oreg. Ltd. partnership, contrary to the finding.

"Services" by a partner are anything of value IN THE JUDGMENT OF THE PARTIES. (Culbertson vs. Commissioner, supra, at page 1215.)

In this case, Mrs. Bronson lived and maintained the residence which was also used as an office on the mill-site, she handled the telephone matters and was in charge while plaintiff was away. She secured employees for the mill and generally did each and everything necessary to help it along whenever called upon.

In addition she entered into the business discussions at the house and entertained the mill customers, and foremost, she was at the mill site and familiar with the employees in the event of injury or casualty to Mr. Bronson, which was of real and substantial interest to Mr. and Mrs. Roles.

Perhaps the most significant contribution to the partnership at its inception (which is the time when the taxable interests of the partners are determined for tax purposes) is that she provided the necessary stability to the partnership. Where Mr.

Bronson's liability as a limited partner was limited to $2,500.00, she had unlimited liability as a general partner. (See Twin Oaks Co. vs. Commissioner, supra.)

She signed the timber purchase contracts with the United States Government long before this partnership was questioned and thereafter became liable on a bond for performance of such a contract.

It has previously been pointed out that "it would be strange also if in so coordinated a family activity, policies involving management, sales and expansion were not discussed and decisions made at the family fireside." (Cooke vs. Glen, supra quoting Lawton vs. Commissioner.)

That this had been a policy among these partners is shown by the fact that although Warrenton Shingle Company was legally a corporation for liability reasons, its growth and development were the combined work, effort and discussion of each of the Parkdale partners who had long treated Warrenton Shingle as a partnership among themselves.

C. PLAINTIFF THROUGH HIS CONTRIBUTION OF CAPITAL AND THROUGH HIS MAN-

AGEMENT OF THE PARKDALE LUMBER COMPANY WAS ENTITLED ONLY TO ONE-FOURTH OF THE INCOME OF THE PARKDALE LUMBER COMPANY.

Plaintiff through his contribution of capital and through his management of Parkdale Lumber Company ACTUALLY created the right to receive and enjoy only one-half of the income therefrom taxed to plaintiff, amounting to one-fourth of the income of Parkdale Lumber Company, Oreg. Ltd., contrary to the finding.

The finding of fact as written is a conclusion and is unsupported by the evidence.

It has been repeatedly held that the RIGHT TO RECEIVE and control the income from the partnership and not the actual control is the determining factor. (Funai vs. Commissioner 181 F. 2d 896.)

There is no evidence in the present case to show that the right to control the disputed one-fourth share of the income was in plaintiff and not in Mildred P. Bronson.

The uncontradicted testimony of the parties that Mildred Bronson had the right to control one-fourth of the income is supported by the fact that

Mildred P. Bronson did actually receive and deposit one-fourth of the partnership distribution and did pay a tax based thereon before this matter was ever questioned by the Commissioner.

Helvering vs. Hoist 61 St. Ct. 144.
Apt vs. Birmingham 89 Fed. Sup. 361.
Funai vs. Commissioner (18 1F 2d 890).

In the Funai case it was said at page 894:

> "There is no rule of law that requires the recipient of money to spend it before it can be classified as income. The *right to control* funds and not the exercise of that right is the valid factor." (Italics ours.)

In the present case, plaintiff had effectively disposed of his interest in any capital contribution of the parties and hence his right to control the same. Legally, morally, and intentionally, he acquired only a one-fourth interest in the concern.

If the parties join together in the conduct of business and agree that the services or capital to be contributed by each are of value to the partnership, that is sufficient. The government will not be permitted to submit its judgment for that of the parties. Culbertson vs. Comm. Supra, page 1215.

In the present case, the judgment of Richard and Janet Roles and plaintiff was that the services

of Mildred P. Bronson were of value to the partnership, and they willingly accepted her as a member of the partnership.

Services need not be clerical, manual or physical, but may be in the nature of business discussions of policy around the family fireside or at any other place. Cooke vs. Glen, Supra.

Persons in partnership have a right to choose their business associates and if such person contributes in stability or any other manner in the judgment of the partners, that should be sufficient. Culbertson vs. Commissioner, (Supra); Hair, Chester, Ballington vs. Arnold, (501 USTC par. 9255).

Here there is no evidence that would allow the Commissioner to substitute his judgment for that of the other three partners in this respect.

D. PLAINTIFF ACTUALLY RECEIVED OR ACTUALLY CONTROLLED AND TREATED AS HIS OWN ONLY ONE-FOURTH OF THE INCOME OF THE PARKDALE LUMBER COMPANY TAXED, FOR FEDERAL INCOME TAX PURPOSES TO HIM.

Plaintiff did not actually receive or control and

treat as his own all of the one-half of the income of Parkdale Lumber Company, Oreg. Ltd. taxed for federal income tax purposes to him, contrary to the finding.

The evidence discloses that the distributions of income from Parkdale Lumber was distributed by individual checks to each of the members of the partnership in like amounts and that the checks when so deposited were placed in the only personal account maintained by plaintiff and his wife which was jointly controlled.

Drawings from this account were made by both plaintiff and defendant, and it should be pointed out that there is no showing that plaintiff ever withdrew from that account more than his share of the deposits made by him thereto, on which he had reported and paid income taxes.

We have previously discussed in the last preceding specification the question of ownership from right to control.

E. THE PARTNERSHIP ARRANGEMENT KNOWN AS THE PARKDALE LUMBER COMPANY MADE A SUBSTANTIAL CHANGE IN THE ECONOMIC RELATIONSHIP OF PLAINTIFF AND

HIS WIFE: HE DID NOT CONTINUE TO EARN AND PRODUCE THE INCOME TAXED TO HIM AND DID NOT CONTROL ITS USE AND DISPOSITION.

The evidence discloses that the economic relationship of plaintiff and his wife was changed as a result of the formation of Parkdale Lumber Co. and that plaintiff did not continue to earn and produce the income taxed to him and control its use and disposition, contrary to the finding.

The fallacy in proposed finding No. 6 is that at the inception or formation of Parkdale Lumber Company, Oreg. Ltd. there was no economic relationship to income which could be the subject of change, since at that time there was no income.

At the inception, the economic relationship of plaintiff and his wife was changed, however, by the exposure of their assets to the hazards of the Parkdale Lumber Company operations or liabilities which at that time consisted of the balance due on the purchase price of the mill and whatever additional indebtedness might be created by the action of the other partners in connection with the operation. Twin Oaks Co. vs. Commissioner (183 Fed. 385, 387).

It should be apparent that this finding has no relation to the question presented since at the formation there was no income which could be the subject of economic changes.

It should be pointed out that in every case where a member of a family is a partner in a business that there is no change in the economic relationship of the family as to income even if the wife is the controlling and dominent influence in the partnership and had invested all of the capital.

Plaintiff could not *continue* to produce income of the Parkdale business since neither he nor any other member of the partnership had produced any income when the partnership was formed.

This finding seeems to indicate the misconception of the court concerning the fundamental question of intent to form a partnership.

This finding was undoubtedly taken from the case of Commissioner vs. Tower, 148 F. 2d 388, where a husband gave his wife an interest in an existing business and where wife did not share in the distribution, it was held that there was no change in the economic relationship of the family to income by virtue of the transfer. That was the

typical tax avoidance family partnership arrangement where the husband CONTINUED as he had done before to earn the income and to control distribution of its profits. This has no relationship to the present case factually or legally.

The Supreme Court in discussion of the Tower case in the later case of Culbertson vs. Commission, Supra, stated at page 1215:

> "Unquestionably a court's determination that the services contributed by a partner are not vital, and that he has not participated in management and control of the business or contributed original capital has the effect of placing a heavy burden on taxpayer to show a bona fide intent of the parties to join together as partners. BUT SUCH A DETERMINATION IS NOT CONCLUSIVE AND THAT IS THE VICE IN THE "TESTS" ADOPTED BY THE TAX COURT. IT ASSUMES THERE IS NO HONEST DIFFERENCE OF OPINION AS TO WHETHER THE SERVICES OR CAPITAL ARE OF SUFFICIENT IMPORTANCE TO JUSTIFY HIS INCLUSION IN THE PARTNERSHIP." (Emphasis ours.)

This assessment was made long before the decision in the case of Culbertson vs. Commissioner but after the Tower case.

In the present case, we are determining the question from the standpoint of four people not

members of the same family but of two families.

F. MILDRED P. BRONSON DID INFLUENCE THE CONDUCT OF THE BUSINESS OF THE PARKDALE LUMBER COMPANY AND EXERCISED VOICE AND CONTROL OF THE DISTRIBUTION OF THE INCOME OF THE BUSINESS.

The evidence discloses that Mildred Bronson did influence the conduct of the business of Parkdale Lumber Company, Oreg. Ltd., and did exercise voice and control of the distribution of the income of the business, contrary to the finding.

The only evidence in the case indicates that Mildred P. Bronson took an active part in the general discussions of the business problems, lived at the site of the operation, her home was used for its office, signed documents relating to its purchase of timber from the Forest Service and willingly agreed to be a general partner in the business. She was called upon to hire employees and to know the personnel of the mill. She had been continuously consulted concerning the desirability of purchasing the mill and other investments and had discussed over the previous years each of the opera-

tions of the previous business. She did not live in the penthouse in the city but in the woods at the mill site where the business discussions took place.

There is no evidence that she did not so participate and no evidence to support the conclusions that she failed to influence the conduct of that business, and no evidence that she failed to exercise any voice or control over the distribution of the income. The facts prove she did along with the other partners receive the income at irregular distribution dates.

G. PLAINTIFF AND R. C. ROLES DID NOT ACTUALLY CONTROL AND DOMINATE THE BUSINESS OF THE PARKDALE LUMBER COMPANY.

No evidence supports the conclusion contained in the findings of fact to the contrary.

Mr. Bronson took an active part in the management of Parkdale Lumber Company, as did Mr. Roles, but all of the evidence is to the effect that all four partners met frequently, personally and by telephone, to discuss business affairs.

There is no evidence from which it can be said that "we apportion the control and domination to Mr. Roles and plaintiff."

We assume, but not without some doubt that the male is or believes he is somewhat more dominant than the female, but we find no proof of this in the evidence of this case nor elsewhere, nor is this fact controlling. (Apt. vs. Birmingham, supra page 381.)

The fallacy in this finding is apparent when we consider that a partnership in the conduct of its business might be in truth, and indeed often is, dominated by a hired employee. The fact, if true, has no relation to the problem at hand in any event.

Here again we are concerned not with domination but with the right to dominate, or control, whether exercised or not.

The parties here intended the consequence of their act and that was to conduct mutually a business for profit.

The RIGHT to control this partnership was vested in Mildred Bronson and R. C. Roles and not in the limited partners.

H. FROM A CONSIDERATION OF ALL THE PLEADINGS THE PRE-TRIAL ORDER AND ALL OF THE EVIDENCE IN THE CASE ORAL

AND DOCUMENTARY, INCLUDING THE PARTNERSHIP AGREEMENT, THE CONDUCT OF THE PARTIES IN THE EXECUTION OF ITS PROVISION, THEIR STATEMENTS, THE TESTIMONY OF ALL THE WITNESSES, THE RELATIONSHIP OF THE PARTIES, THEIR RESPECTIVE ABILITIES AND CAPITAL CONTRIBUTIONS, THE ACTUAL CONTROL OF THE INCOME AND THE PURPOSES FOR WHICH IT WAS USED AND ALL OTHER FACTS AND CIRCUMSTANCES THROWING LIGHT OR TENDING TO SHOW THE TRUE INTENT OF THE PARTIES TO THE AGREEMENT THAT PLAINTIFF AND HIS WIFE DID INTEND IN GOOD FAITH AND WITH A BUSINESS PURPOSE TO JOIN TOGETHER AS PARTNERS IN THE CONDUCT OF THE BUSINESS OF THE PARKDALE LUMBER COMPANY.

The evidence indicates that the parties themselves did intend to and did in fact enter into a bona fide partnership for a business purpose in the conduct of the business known as Parkdale Lumber Company, Oreg. Ltd., contrary to the finding.

To conclude that the parties (the finding only refers to two of the partners) did not intend to

form a partnership from the facts proven by the evidence would be to totally disregard the testimony of the parties comprising the partnership and the testimony of the only disinterested witness, and all of the documentary evidence. There were no witnesses for the Government.

The testimony of the parties was that they did intend to form a bona fide partnership. It seems so irrefutable as to be a matter of law "that a person intended the natural consequences of his voluntary acts." This is made a presumption under the laws of the State of Oregon and is set forth as quoted above in Oregon Compiled Laws Annotated, Section 2-407 (2). Their being no evidence to the contrary the presumption stands.

All of the parties being of legal age and competency executed documents by which the partnership was formed and caused those articles to be publicly recorded pursuant to law. Their insurance policy was so worded and published; their contracts with the Government bound them in that capacity.

It is difficult to see how the Commissioner under such circumstances can arbitrarialy state "you did not intend the natural consequence of your act;

you did not intend to form a partnership."

This matter was not a spur-of-the-moment transaction. The partners had taken several months to look for a new investment after the disastrous fire of the late fall. They were certainly not concerned with a transfer of interests in an existing business for the purpose of avoidance of taxes at that point when they had not even found an investment.

Even prior to consultation with Mr. Martin whom they consulted primarily in connection with Workmen's Compensation Insurance, they decided on the formation of the partnership arrangement.

Let us assume that at this point (although it is contended to the contrary) that the sole purpose of choosing this form of business entity was for the express and only purpose of reducing or minimizing income taxes if the business were successful.

All decisions respecting this question recognize that this purpose is not only a legitimate but a proper motive for selecting a particular type of business entity, either at the formation or even while in operation.

(Commissioner vs. Tower, Supra; Vaughn vs. Carey, 88 F. Sup. 967.)

We can therefore eliminate the tax saving motive either on the ground that it is proper or on the ground that at the formation of a new business where there is then no income, there can be no motive to save taxes. Certainly it would not reduce Mr. and Mrs. Roles' profit to have Mrs. Bronson as a partner irrespective of taxes.

If the sole motive therefore is not to minimize taxes or if the tax saving motive is proper, then on what other ground can the Commissioner determine that there is no intent to form a partnership. The answer to this question is that the Commissioner has no other ground for making the challenge, and if the partnership is valid, it is valid for tax purposes.

The partners certainly intended to form a partnership and entered into that arrangement.

The closest reported case factually to the one at present where the question was raised is Cooke vs. Glen, Supra, which held in favor of the taxpaper.

I. PLAINTIFF'S WIFE WAS INCLUDED IN THE BUSINESS CONDUCTED AS THE PARKDALE LUMBER COMPANY AS A PARTNER FOR

A GENUINE BUSINESS PURPOSE. SHE WAS NOT BROUGHT INTO THE BUSINESS.

The finding again appears to disclose the misconception of the court concerning the fundamental question of intent to form a partnership.

The evidence shows that no partners were "brought into" an existing business but this was a new business venture in which all of the parties were interested prior to starting its operation.

Finding numbered 10 assumes a bringing in "of a partner to an existing business." Such an assumption is completely unsupported by the evidence. There is no evidence that Parkdale Lumber Company operated even a short period of time before plaintiff's wife was included as a member of the partnership. Plaintiff's wife was a member of the partnership from its formation and prior to its operation.

Mrs. Bronson was made an original partner to provide stability through general liability and to protect the interest of the other partners in the event of a casualty to her husband in a hazardous occupation, and to be familiar with the operation and advise and consult in its conduct and opera-

tion. She was not "brought in" for minimizing plaintiff's income taxes, since there had been no income from this source at the time the partnership was formed, nor was she ever "brought in." She was an original partner.

It should be remembered that if Mrs. Bronson was "brought into the partnership," it would be by others than a member of her family. For a partner can not be made a partner against the will of the others.

J. ASHBAUGH WOOD SHINGLES AND SHAKES WAS NOT ORGANIZED TO PERMIT PLAINTIFF AND R. C. ROLES TO AVOID O. P. A. REGULATIONS. THEIR WIVES WERE MADE ACTUAL PARTNERS IN THE ENTERPRISE, AND PLAINTIFF'S WIFE HAD DOMINATION AND CONTROL OVER THE INCOME ALLOCATED TO HER.

The evidence shows that the plaintiff had no interest in the Partnership known as Ashbaugh Wood Shingles and Shakes, exercised no control thereover, had no right to control the business activities of that concern and could not be taxed on the income from that source.

As has been previously pointed out, when a person, even where he had a previous interest in a business, divests himself of that interest, so that he no longer has the right to control the activity thereof, nor the investment therein, then the earnings or income therefrom are no longer taxable to him.

Since he has nothing to assign, he can not be taxed as a sham assignor.

Here again there could be no purpose of income tax minimization at the inception of the contract since at that time, there was no income to minimize from this source.

The Government received the taxes on the income derived from this source when Mrs. Bronson properly reported them and paid a tax thereon.

The Government's contention appears to be that this was actually the income of the corporation producing the shingles sold by the partnership.

The case of Twin Oaks Co. vs. Commissioner, Supra, decided by this court holds directly contrary to this contention on far weaker facts than presented here.

The case of Fahnrich vs. Paulsen (134 Ore. 247, 293 Pac. 422) holds that a corporation may not become a partner.

Here the Warrenton Shingle Company had refused to ship shingles to Mr. Stark because their output was previously sold, but they were willing to and did ship shingles to Ashbaugh who was a long-standing customer of theirs. When Ashbaugh sold his business, the corporation continued to ship shingles as before. The corporation did not change its position in any way. The idea of Mr. Stark to assure his supply by voluntarily including Mrs. Bronson and Mrs. Roles in this partnership did not change the position of Warrenton Shingle Company in any way.

It was of obvious advantage to Mr. Stark to have Mrs. Bronson and Mrs. Roles as partial beneficiaries of the income from his business, and from his deposition, exhibit 129, it appears that he considered that the supply of shingles would at least be continued to him on the same basis as prior if he purchased the Ashbaugh business.

There were no promises made to him concerning this supply, and in fact, his supply was termi-

nated when he failed to pay a $3000.00 account to the Warrenton Corporation.

Mr. Bronson certainly contributed nothing to this concern toward the production of the income, and was certainly not a partner therein formally or informally.

For taxation purposes, there is no theory on which it could be said he did dominate and control the income allocated to Mrs. Bronson.

She received all of the checks and there is no showing that she did not exercise every right of ownership and control incident thereto.

There is no showing that plaintiff ever exercised any control or domination over any income from this source.

We again call attention to the holdings that when a person or a corporation effectively divests itself of control or ownership in a business, the divestor is not thereafter taxable on the income therefrom.

So that even were we to assume that this was the income of the corporation as contended by defendant, having divested itself of any interest or control thereof, the corporation or its stockholders

would not be taxable on the income therefrom. (Twin Oaks vs. Commissioner, Supra; John L. Denning Co. Inc. vs. Commissioner, Supra.)

CONCLUSION

I.

Plaintiff contends that the evidence establishes the following essential facts as to Parkdale Lumber Company.

1. A new and untried business venture.
2. A legal limited partnership.
3. Contribution of capital by all partners.
4. Contribution of services by all partners.
5. Bona fide intent to form a partnership by all partners.

If these are proven, then there can be no other judgment than in plaintiff's favor.

There appears to be no dispute as to the first two of the above facts.

As to "contribution of capital" the court's error appears to be predicated in its failure to consider the fact that capital may be acquired by gift or loan. The court held that Mrs. Bronson contributed no capital. Yet the evidence supports only one con-

clusion — that she did contribute $2500.00.

As to contribution of services, the court's error appears to be predicated on its failure to properly evaluate "services."

Services need not be manual, clerical or physical but may consist of advice, stability, consultation or any other things which is IN THE JUDGMENT OF THE PARTNERS, of value.

There can be no other conclusion drawn from the evidence than that services were contributed by all of the partners.

As to intent to form a partnership, there is no evidence from which it can be said that the parties did not intend to form the partnership. Every act and every exhibit shows to the contrary.

The allocation was arbitrary and capricious and plaintiff is entitled to a refund of the taxes paid as a result of the allocation of an additional one-fourth of the Parkdale Lumber Company, Oreg. Ltd. income to him for the years in question.

II.

Plaintiff contends that the evidence establishes the following essential facts as to Ashbaugh Wood

Shingles and Shakes.

1. That plaintiff made no capital investment in that concern.

2. That plaintiff contributed no services to that concern.

3. That plaintiff had no right of management or control of the policies of that concern.

4. That plaintiff had no right to control the income from that concern.

5. That plaintiff had no legal, or equitable or moral interest in that concern.

These facts all appear not to be in dispute.

The court's error appears to be in a failure to understand or apply the law relative to the taxability of income from a source in which the taxpayer in no way participates.

The Government's contention as to Ashbaugh is the direct opposite of their contention as to Parkdale.

We are here interested only in the question of taxability of income.

There is no basis for taxing income to the plaintiff from this source.

The allocation was arbitrary and capricious and plaintiff is entitled to a refund of taxes paid as a result of the wrongful allocation of the income from Ashbaugh Wood Shingles and Shakes previously reported by Mildred Bronson.

Respectfully submitted,

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